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In This Issue

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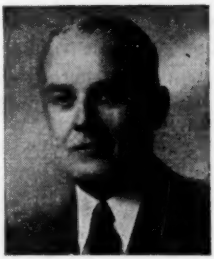
THE PRESIDENT'S PAGE

JUNIOR BARRISTERS OF THE LOS ANGELES BAR ASSOCIATION



Dana Latham

THE organization meeting of the group now known as the Junior Barristers was held May 24th, 1928. Hubert T. Morrow, then President of the Los Angeles Bar Association, sparked its formation. Its objects and the nature of its organization were determined by popular vote of the 145 young lawyers who attended that first meeting. Its aims were stated in its first annual report issued in 1929 as follows:

> "To stimulate and promote the young lawyers' acquaintance among the members of the Bar and the occupants of the Bench; to form an available working unit which can be used to help carry out the plans of the Bar Association; to hold meetings at which addresses and discussions on subjects of special interest to men new in the profession may be heard and participated in; to promote among its members especially, and among members of the Bar generally, high standards in practice and respect for and understanding of the ethics of our profession; to do what it can for the welfare of young lawyers in Los Angeles County."

Charles E. Beardsley, now Chairman of the Association's Committee on Constitutional Rights, was its first chairman. Our Senior Vice President, Herman F. Selvin, and one of our Trustees, William T. Coffin, were among its organizers.

Over the years the Junior Barristers have become an integral and exceedingly important part of the Los Angeles Bar Associa-

tion. Article VIII of the Association's By-Laws now specifically provides for a standing committee to be known as "Junior Barristers of the Los Angeles Bar Association." This committee consists of all male members of the Association who have been admitted to practice by examination within the preceding seven years, provided, however, that no one shall be eligible for membership on this committee if he is over 35 years of age. The dues of the Junior Barristers are graduated according to the length of time they have been admitted to the Bar. It has its own by-laws and its chairman is a member of the Board of Trustees of the Association.

The Junior Barristers hold their own monthly luncheon meetings which are customarily addressed by some older member of the local Bar on some problem of special interest to the younger lawyers. The Junior Barristers also hold an annual stag Frolic which it is understood their elder brothers would love to attend.

This committee performs a most important function within the local Bar. Not only does it serve as a means of introducing newly admitted lawyers into Bar Association activities, but it performs yeoman service for the Association as a whole.

Every committee of the Bar Association has one or more Junior Barristers on its roster. The contribution of these younger members has been great. In particular they have been ready, willing and able to undertake and complete projects impossible of achievement by the older lawyers.

At present some 316 members of the Association are members of the Junior Barristers. It is the fond hope of the Trustees and officers of the Association that this number will constantly increase. The area of achievement possible to this group is almost without limit.

This issue of the Bulletin, which is being edited exclusively by the Junior Barristers, will be, as has always been the case, one of the best issues of the year.

I am sure that all the older members of the Association join with the officers and Trustees in congratulating the Junior Barristers upon their fine accomplishments and wishing them all success in the future.

DANA LATHAM

A WORD FROM THE CHAIRMAN OF THE JUNIOR BARRISTERS

Edward C. Freutel, Jr.

ONCE again we Junior Barristers have occasion to display before our elders such erudition as we can muster. This issue is entirely the work of members of the Junior Barristers. We are grateful to the Board of Trustees and to the Bar Bulletin Committee for the opportunity to produce it. We hope that you will conclude that we have done what Professor Edward H. (Bull) Warren would have called a "lawyerlike job."

In keeping with the precedent established last year, a contest was held to determine the best article submitted for this issue,* and the winner will be awarded a plaque. The victor is William A. Cruikshank, Jr. His article, entitled, "California's Marital Exemption and Its Effect Upon the Inheritance Tax Law," was selected by a panel of judges composed of the Honorable Louis C. Drapeau, Herman F. Selvin and Loyd Wright. We appreciate their kindness in serving in that capacity and trust their task was not unduly onerous.

Junior Barrister Editor-in-Chief Phil Westbrook and his associate editors have worked long and arduously to produce this issue and a large measure of the credit for the material which follows is justly theirs. The names of the editors appear on page 11.

We are glad to report that our post-war resurgence continues unabated. Eighty-two new members have joined our ranks since the beginning of this year. Junior Barristers serve actively on each of the Association's Committees and have responded enthusiastically to calls for varied forms of special assistance in connection with the Association's affairs.

It may interest you to know that on July 22 we renewed for the first time since the war the tradition of a combined lawyer-doctor celebration. Members of the Junior Section of the Los Angeles County Medical Association joined us at the Chevy Chase Country Club for an agreeable afternoon devoted to beer, good-fellowship and attendant delights.

EDWARD C. FREUTEL, JR.

*The articles entered in the contest were submitted to the judges without the revision and editing which they have received by their authors and the editors in preparation for publication.

CALIFORNIA'S MARITAL EXEMPTION
AND ITS EFFECT UPON THE INHERITANCE TAX LAW*

By William A. Cruikshank, Jr.**

William A. Cruikshank, Jr.

THE federal estate tax law was amended in 1948 to allow the deduction from the taxable estate of an amount equal to the value of the separate property left by a decedent to his surviving spouse. The right to this deduction was qualified by many conditions as to the nature of the interest passing to the spouse, and the maximum deduction was limited to one-half the decedent's separate property (or pre-1927 California community property). The announced policy behind the incorporation of such a concept into the estate tax law was the recognition of the spouses as an economic unit.[1] Like the community property system, the marital deduction gave tax credence to the theory that one-half of the family's property "belongs to" and is contributed by the efforts of each spouse. Thus, only "his" half of the property should, realistically, be taxed in the husband's estate, while the other half will be taxed at the wife's death. With the aid of the lengthy statute and regulations put forth to enunciate this new provision and numerous explanatory commentaries, the deduction is now accepted as almost comprehensible to those who must deal with it.

As soon as the federal law could be examined and its tax-saving possibilities realized, there arose a movement in some of the states for the adoption of a similar measure in their death tax patterns. On April 11, 1950, New York obliged with an enactment almost identical with the federal deduction.[2] Then Governor Warren signed a bill on April 26, 1950, which immediately pro-

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*This article was selected as the best article on a current legal subject submitted for the Junior Barristers' contest. See page 3, *supra*, for details.

**William A. Cruikshank, Jr., born 1923; LL.B., University of Southern California, 1949. Military service with United States Army Air Corps, 1942-1945, 1st Lt.; Associated with Alva C. Baird.

[1]This legislation was also induced, in large measure, by demands that all persons be treated fairly and without discrimination irrespective of whether they lived in a community property or a common-law State. See *Report of Senate Committee on Finance*, SEN. REP. No. 1013, 80th Cong., 2d Sess. (1948), 1948-1 CUM. BULL. 285.

[2]N. Y. Laws 1950, c. 585, originally introduced on January 30, 1950, as Assembly Bill No. 1273. The text of this law is available in 3 P-H INH. & TRANSFER TAX SERV. ¶1185 (Ed.), N. Y. Inh. ( ). It becomes effective on October 1, 1950.

vided a marital exemption under the California inheritance tax law. Before examining the provisions of the California law and the distinctions between it and the marital deduction under the federal estate tax, it may be interesting to consider the motives behind the current legislative activity.

I.

REASONS FOR A STATE MARITAL DEDUCTION OR EXEMPTION

The primary justification for lenient tax treatment of property transfers between spouses is the premise that the family constitutes an economic entity.[3] The states should be no more unrealistic in this regard than the Federal Government which has given partial effect to this principle through the marital deduction and the "split-income" provisions of the current income tax.[4]

States may also be induced to follow the federal tax program by the practical problems of tax administration. Indeed, insofar as possible, California and New York have endeavored to conform their tax laws with the federal statutes.[5] In that way, the wealth of federal rulings and decisions is available to aid in the interpretation of the intricate provisions which are common to the several taxing jurisdictions. The rapidly produced quantity of federal interpretations serves to facilitate the solution of many problems which would not reach the state appellate court level for many years. Moreover, a certain uniformity of rule and interpretation, a common law of taxation, if you please, is achieved by this process of "follow the leader."

New York was also influenced by a marital deduction recommendation[6] which stated that, without such relief, wealthy resi-

[3]See Surrey, *Federal Taxation of the Family*, 61 HARV. L. REV. 1097 (1948).

[4]INT. REV. CODE §§12(d), 51(b), as amended by Revenue Act of 1948.

[5]California, it is true, has an inheritance tax, while New York and the Federal Government impose estate taxes. The bases of the taxes and the technical provisions, however, are quite similar. Peculiar problems of statehood made it impossible to impose such sweeping measures in some instances as are contained in our federal tax laws. The underlying efforts to follow the federal provisons are, nevertheless, readily apparent.

That judicial interpretations of federal tax laws should be followed in applying California revenue measures, see Holmes v. McColgan, 17 Cal.2d 426, 110 P.2d 428 (1941); Borroughs v. McColgan, 21 Cal.2d 481, 133 P.2d 385 (1943).

[6]*Report Recommending That New York Adopt The Marital Deduction*, prepared by representatives of: Section on Taxation, New York State Bar Association; Committee on Taxation, Association of the Bar of the City of New York; Committee on Taxation, New York County Lawyers Association; New York State Bankers Association; Special Committee of New York State Life Underwriters Association.

This report is available in 3 P-H INH. & TRANSFER TAX SERV. ¶1181 (Ed.), N. Y. Inh. ( ).

(Continued on page 20)

SALE OF A RETAIL BUSINESS—
A GUIDE

By John S. Welch*

John S. Welch

IN ONE recent week the *Los Angeles Daily Journal* published 168 notices of intended sale and 50 notices of intention to chattel mortgage, under the Bulk Sales Act — Civil Code Section 3440. Such volume and regularity of use of a legal freeway demand a smooth course and a well posted route. This note is offered as a traffic guide to the hurried traveler.

Because of its admirable qualities of efficiency and security, the escrow is held in high esteem in this state as a lawyer's tool and is customarily and wisely used to complete sale transactions. Problems of buyers and sellers who "go to escrow" are considered herein.

I. THE BUYER

The buyer parts with hard cash and binding promises for the opportunity to go into business. He intends his gamble to lie in the future of the enterprise, not in his acquisition of it. Consequently, the buyer must insist that the seller arrive at the rendezvous with all riders off his back. Specifically, attention should be paid to the following:

A. *Chattel Mortgages.* The sale of a business ordinarily includes the transfer of stock in trade, fixtures, and store equipment. Chattel mortgages may exist upon the stock in trade as well as upon fixtures and equipment. Although turnover of merchandise is ordinarily accomplished on unsecured credit, the seller may have bought the business, giving a chattel mortgage on all property to secure the purchase price. A chattel mortgage search[1] should never be omitted without the buyer's conscious assumption of the inherent risk.[2]

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*John S. Welch, born 1920; B.S., Utah State Agricultural College, 1941; LL.B., Harvard University, 1948. Military service with United States Army, 1941-1946; Major. Associated with firm of Latham & Watkins.

[1]This service is offered by the title companies.

[2]Recordation under CAL. CIV. CODE §2957 protects chattel mortgages otherwise void as to third persons without notice.

B. *Trust Receipts.* Retailers in some lines acquire their merchandise on trust receipt. An entruster's rights are superior to those of a transferee in bulk.[3] Consequently, inquiry as to trust receipt filing should also be made.[4]

C. *Seller's Title.* If the seller owes money on his stock or equipment, it is more likely to be under conditional sales contracts than chattel mortgages. Enforceability of more stringent terms on default,[5] lack of recording requirements,[6] and ease of financing[7] have made the former device more attractive to creditors. A *bona fide* purchaser from a conditional vendee acquires no title.[8]

The seller may have received the merchandise on consignment. By California Civil Code Section 2369 he is given authority to deal with such merchandise as his own, as to persons without notice of the actual ownership.[9] However, it may be that this section does not protect buyers in bulk sales but only transferees in the ordinary course of business.[10] Further, lack of notice of the consignment may be difficult for the buyer to prove.

Other defects of title may also exist by reason of probate proceedings[11] or a petition in bankruptcy.[12]

Consequently, the buyer should make inquiries sufficient to satisfy himself concerning title to the property.

D. *The Lease.* Ordinarily the seller agrees to assign his lease to the buyer as part of the transaction. In some cases the seller has only a month-to-month tenancy, the lease for a term having expired, or never having existed. In others, the lease contains a

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[3]CIV. CODE §§3012 *et seq.*, 3013(1), 3016.5(2)(b). Provisions as to filing must have been complied with.

[4]Write to Secretary of State, Sacramento, California.

[5]Conditional seller may retake chattel without foreclosure and keep the paid installments. Liver v. Mills, 155 Cal. 459, 101 Pac. 299 (1909).

[6]M. P. Moller, Inc, v. Wilson, 8 Cal.2d 31, 63 P.2d 818 (1936); but see CAL. CIV. CODE §2980 requiring recordation of conditional sales of livestock and mining equipment.

[7]Purchase of chattel mortgages by banks is comparatively rare.

[8]Bice v. Harold F. Arnold, Inc., 75 Cal. App. 629, 243 Pac. 468 (1925). Under Martin v. Hollins, 118 Cal. App. 561, 5 P.2d 899 (1931), and Guerin v. Kirst, 33 Cal.2d 402, 202 P.2d 10 (1949), a court may allow retention of the property upon payment of the balance due to the conditional seller.

[9]CAL. CIV. CODE §§2026, 2369.

[10]CAL. CIV. CODE §§2991, 3013(1). See note, 14 A.L.R. 439.

[11]CAL. PROB. CODE §785 (requiring court confirmation of sales).

[12]Under 11 U.S.C. §110, title to a bankrupt's property is in the trustee in bankruptcy from the date of the bankrupt's adjudication.

(Continued on page 28)

THE BURDENS OF PLEADING AND PROOF ON BONA FIDE PURCHASE OF REAL PROPERTY

By Bennett W. Priest*

Bennett W. Priest

ALTHOUGH California attorneys know that the issue of *bona fide* purchase is very likely to arise in any suit involving title to realty, do they realize which party carries the burden of pleading and proof on the issue?

The problem is not easily solved by a hasty search through *California Jurisprudence* or *McKinney's Digest*. The following summary of authorities is an attempt to indicate whether the courts will place the burdens of pleading and proof upon the alleged *bona fide* purchaser or upon his opponent.

The form of the action does not affect the question. The most common situation is an action to quiet title brought either by or against one claiming as, or through, a *bona fide* purchaser. Also, title to realty is directly involved in other forms of action, such as petitions for injunctive relief, and suits to impress a trust upon the realty. The rules as to burden of pleading and proof of *bona fide* purchase are the same in any action involving title to real property.

A. BURDEN OF PLEADING

Suppose an attorney has been requested by a client to clear the title to certain realty. He has been informed that the potential defendant claims to be a *bona fide* purchaser, and he suspects that it will be necessary to prove a defect in the defendant's title such as fraud, undue influence or mistake. What must he plead?

The answer may be found by examining the facts the pleader sets forth in his chain of title. If the pleader sets forth a chain which places the legal or record title in the defendant or his predecessor at the time of bringing suit, the pleader must also outline his attack upon this title in detail.[1] Thus, the facts relating to the

*Bennett W. Priest, born 1923; A.B., University of Southern California, 1944; LL.B., Stanford University, 1949. Military service with United States Navy, 1943-1946; Lieut.(jg). Associated with firm of O'Melveny and Myers.

[1]Pellerito v. Dragna, 41 Cal.App.2d 85 (1940).

defects in the defendant's title and challenging his status as a *bona fide* purchaser by showing notice, lack of consideration or bad faith must be stated in full. Failure to do so subjects the complaint to a general demurrer.[2]

However, if the pleader sets forth a chain of title to the plaintiff which does not indicate a legal or record title in defendant, his complaint is sufficient unto the day. He need not anticipate the defendant's title defense of *bona fide* purchase. The statutory replication supplies his pleading.[3] At the trial he may still attack defendant's chain of title, despite the general rule that fraud, undue influence, or mistake, relied on as a basis of a cause of action, must be alleged in full;[4] here the party is legally entitled to assume that the opponent will not rely on an allegedly frauduent or irreguar transaction.

Furthermore, the failure of the plaintiff to file an affidavit denying the genuineness or due execution of a document pleaded in defense of title[5] does not preclude him from controverting the instrument by any and all other defenses, not inconsistent with the fact of its genuineness and execution.[6]

The attorney's task in pleading will be greatly simplified if he can state the chain of plaintiff's title without showing legal or record title in the defendant. This is usually possible. Or, the plaintiff may simply allege title in himself under a specific instrument of title, and ask for relief against one who claims an adverse interest. In this case, the defendant must plead his title, and the statutory replication will serve as plaintiff's denial and defense. The attorney cannot assume at this point, however, that he will not have the burden, on his case in chief, of overcoming the effect of defendant's chain of title, because later pleadings may show legal title in the defendant.

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[2]Huntoon v. Southern Trust & Commerce Bank, 107 Cal.App. 121 (1930).
[3]Moore v. Copp, 119 Cal. 429 (1897); Watson v. Poore, 18 Cal.2d 302 (1941).
[4]"Until the defendant Marshall filed her answer the plaintiff could not know that the defendant was going to rely upon the deed pleaded in the answer of the defendant. After that answer had been filed the statute neither authorized nor required the plaintiff to file another pleading in the nature of a replication. However, at the trial the plaintiff was entitled to attack the deed held by the defendant on the ground that it was not supported by any consideration . . ., or that it was forged . . . or that it was obtained through fraud . . ." Lewis v. Marshall, 90 Cal.App. 351, 354 (1928); see also Bertelsen v. Bertelsen, 49 Cal.App.2d 479 (1942).
[5]CAL. CODE CIV. PROC. §462.
[6]Miller v. McLaglen, 82 Cal.App.2d 219 (1947).

(Continued on page 34)

CURRENT CASES

SUFFICIENCY OF USE TAX RETURN TO START STATUTE OF LIMITATIONS RUNNING AGAINST STATE

When is an incomplete sales or use tax return sufficient as a report of tax liability to start the statute of limitations running in favor of the taxpayer? The California Supreme Court answered the question in *People v. Universal Film Exchanges,* 34 A.C. 726 (1950). A retailer had filed combined sales and use tax returns in which entries appeared under sales tax sub-headings but in which use tax sub-headings were left blank. In a suit by the State of California to recover use taxes for the periods during which the above form of tax returns had been filed, the Supreme Court reversed the trial court and District Court of Appeal and *held,* the state's action was barred by the statute of limitations, because the blank use tax return satisfied the law as a report of use tax liability.

The neglect or refusal of the taxpayer to file any tax return at all, will not, of course, start the statute of limitations against assessment of taxes. The statute will be tolled by a return which, although complete in form, is filed with intent to defraud, or to evade payment of due taxes, or is "misleading and calculated to prevent discovery of material facts." *John D. Alkire Inv. Co. v. Nicholas,* 114 F. (2d) 607 (1940); CALIF. REV. & TAX. CODE Section 6487. A "sufficient return" is not made by a taxpayer when he does not intend his report to comply with the statute, nor by his filing a single return when separate returns, containing almost identical information, are required by the taxing authorities, *Hewitt v. Bates,* 297 N.Y. 339, 78 N.E. (2d) 593, 3 A.L.R. (2d) 642 (1948).

However, perfect accuracy and completeness are not necessary to start the statute of limitations running against a return filed in good faith. Thus, a return made on a wrong form but containing all necessary data to compute the tax, has been held sufficient. *Germantown Trust Co. v. Commissioner,* 309 U.S. 304, 60 S. Ct. 566, 84 L. Ed. 770 (1940). Similarly, a valid return was found

in the filing of a tax report on plain paper instead of the appropriate governmental printed form. *Denman v. Motter,* 44 F. (2d) 648 (D.C. Kan., 1930). In holding that a sufficient use tax return had been filed in the principal case, the Court determined that the taxpayer's failure to fill the blanks of the tax form under the circumstances "represented, as clearly as the notation of a 'zero' or the writing of the word 'none,' " a positive declaration that no taxes were due. This result is contrary to the only other discovered decision in point, *Whitmore Oxygen Co. v. Utah State Tax Comm.,* 196 Pac. (2d) 976 (Utah, 1948).

Retailers caught in today's maze of overlapping and seemingly endless sales, use, license, and other municipal and state taxes, and taxpayers long confounded by a plethora of taxing regulations, will applaud as fair and practical the result reached in the principal case. Attorneys may well find in this decision the moral that when a taxpayer in good faith complies with technical requirements in filing his tax returns, the risk of mistaken interpretation of his entries will properly be cast upon the taxing authorities.

IRA M. PRICE, II.

NECESSITY FOR ACTUAL DAMAGES TO SUSTAIN PUNITIVE AWARD

IN *Finney v. Lockhart,* 35 A. C. 182 (1950), an action for maliciously inducing persons not to purchase plaintiff's product, an award of $1.00 for actual damages was held adequate to sustain a punitive award of $2,000. The Court recognized that as a general rule, no punitive or exemplary damages may be awarded unless there is at least some actual or compensatory damage, which must be segregated by the trier of facts from the punitive award. *Mother Cobb's Chicken Turnovers, Inc. v. Fox,* 10 Cal. (2d) 203 (1937); *Haydel v. Morton,* 8 Cal. App. (2d) 730 (1935). In special cases, actual damage may be presumed, as, for example, in an action for defamation where the words are actionable *per se.* In such a case no segregation between actual and punitive damages is required, for the single award, although stated to be solely exemplary, will be presumed also to be compensatory in nature. *Clark v. McClurg,* 215 Cal. 279, 81 A.L.R. 908 (1932).

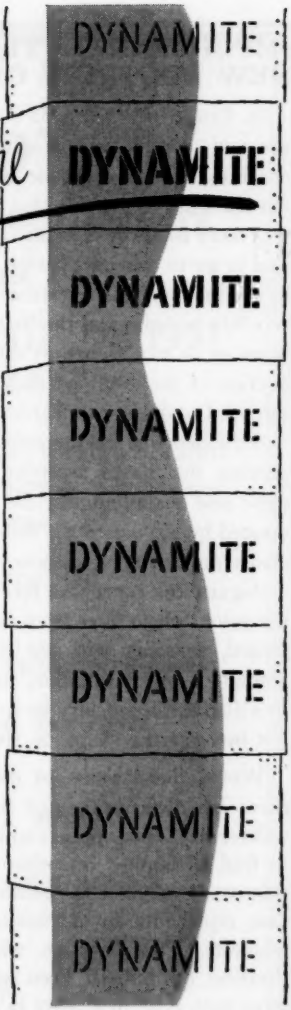
The oft-repeated rule that exemplary damages should bear a reasonable relation to the actual damages, is merely a guide to guard against excessive punitive awards. *Brewer v. Second Baptist Church,* 32 Cal. (2d) 791 (1948). There is no fixed ratio which determines whether the punitive damages are excessive, and the Supreme Court in the *Finney* case cited two defamation cases in Missouri where the disproportion was even greater: *State v. Shain,* 341 Mo. 733, 108 S.W. (2d) 351 (1937), $1.00 nominal damages, $4,000 exemplary; and *Edwards v. Nulsen,* 347 Mo. 1077, 152 S.W. (2d) 28 (1941), $1.00 nominal damages, $25,000 exemplary.

In *Crowell-Collier Publishing Co. v. Caldwell,* 170 F. (2d) 941, 944 (1948, C.C.A. 5th), the court overturned an award of $237,500 damages for publication of a magazine editorial imputing indifference to the Governor of Florida to a lynching in his State, and suggested that appellee seek a change of venue, stating:

> "It is a general rule of law, more strictly observed in some jurisdictions than in others that the punitive power of the jury is not unrestrained but is to be exercised with discretion, and that exemplary or punitive damages awarded must bear some, though not an exact relation to actual damages."

Jury verdicts, in the long run, would probably be more just if this declaration were heeded in this State.

JACOB SWARTZ.



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IMPLIED INTENTION OF TESTATOR—NEW DOCTRINE OF CY PRES?

In *Estate of Akeley,* 35 AC 26, (1950), testatrix' will left "all the rest, residue and remainder" of her estate to three named charities, 25% to each one. Nothing was said of the fourth 25%, but the will did provide that if the total of the designated bequests was more than could legally be given to charity, the excess amount was to go to a named person with the request that he distribute it in the manner that testatrix should have indicated to him. Testatrix left no heirs and the State of California asserted that she died intestate as to a fourth of the estate, and accordingly claimed that portion of the estate by escheat. The court held that the testatrix intended to dispose of her entire estate under the residuary clause, and divided the residue equally among the three charities named. Against the State's assertion that the use of the percentages was clear and unambiguous, the court found that an ambiguity was created by the use of the these percentages in conjunction with the clause purporting to dispose of the entire estate. Having found an ambiguity the court was free to resolve it in accordance with what the court felt to have been the testatrix' intent. Two Justices dissented, agreeing with the State's contention that there was no ambiguity and stating that, just as the court was powerless to write in a further beneficiary as to the undisposed 25%, so also it could not increase the shares to the named beneficiaries to 33⅓%.

Would the decision of the court have been the same had the three beneficiaries named been private individuals? If so, the California Court appears to have overcome its previous reluctance to find an implied intention of a testator. If it is concluded that this result was reached because the beneficiaries were charities, the case represents an extension of the *cy pres* doctrine to outright bequests. That doctrine, which was not once mentioned in the decision, has hitherto been regarded as applicable only where there have been gifts to charity in trust. In the recent case of *Estate of Butin,* 81 Cal. App. (2d) 76 (1947), the Court applied the *cy pres* doctrine even though no trust was mentioned in the will. The Court, however, did say that the executors were really trustees. In the *Akeley* case no attempt was made to find a trust.

HAROLD S. VOEGELIN.

RIGHT TO SEARCH WITHOUT WARRANT EXTENDED

In *United States v. Rabinowitz*, 94 L.Ed. 407 (1950), the right to search without benefit of a search warrant was broadened and extended by a divided decision of the United States Supreme Court. The federal officers obtained a valid warrant for the arrest of the defendant, charged with selling and having in his possession forged and altered government stamps. The defendant was arrested in his place of business, which was a one room office open to the public. The officers thereupon searched the desk, safe and file cabinets from which they seized a number of such stamps. Evidence indicated that arresting officers had sufficient time to secure a search warrant. The Trial Court convicted the defendant of selling, possessing and concealing forged and altered obligations of the United States with intent to defraud. Evidence pertaining to the stamps seized in the search had been admitted by the Trial Court over timely objection of the defendant. Relying on *Trupiano v. United States*, 334 U.S. 699, 92 L. Ed. 1663, 68 S. Ct. 1229 (1947), the Court of Appeals of the Second Circuit reversed the Trial Court.

A five-justice opinion authored by Mr. Justice Minton declared that the only mandate of the Fourth Amendment was that the people shall be secure against unreasonable searches, and that reasonableness of the search is in the first instance for the Trial Court to determine. Furthermore, the court held the search and seizure reasonable primarily because they were incident to a valid arrest, and announced that the relevant test is not whether it is reasonable to secure a search warrant, but whether the search was reasonable. To the extent that the *Trupiano* case required a search warrant solely upon the basis of the practicability of procuring it, that case was expressly overruled. The reversal of the court's former position is emphasized by the fact that in *Rabinowitz* an actual search was necessary to disclose the articles seized, whereas in *Trupiano* seizure was made only of articles visible to arresting officers at the scene.

Mr. Justice Frankfurter wrote a vigorous dissent, with which Justice Jackson concurred. The major premise of the majority opinion, he stated, was that an arrest creates a right to search the

place of arrest. This rule does not find support in the cited decisions of the majority, such as *Weeks vs. United States,* 232 U.S. 383, 58 L. Ed. 652, 34 S. Ct. 341 (1914); *Amos vs. United States,* 255 U.S. 313, 65 L. Ed. 654, 41 S. Ct. 266 (1921); *Byars vs. United States,* 273 U.S. 28, 71 L. Ed. 520, 47 S. Ct. 248 (1927); and *Taylor vs. United States,* 286 U.S. 1, 76 L. Ed. 951, 52 S. Ct. 466 (1932). Study of these cases would seem to bear out Justice Frankfurter's statement that there has been uncritical confusion as to (1) the right to search the person arrested and articles in his immediate physical control, (2) the right to seize visible instruments or fruits of crime at the scene of the arrest, and (3) an alleged right to search the place of arrest. Justice Frankfurter's opinion stressed the importance of carrying out the convictions of the framers of the Constitution, as spelled out in the Fourth Amendment. It is there written, says the dissent, "that law enforcement does not require the easy but dangerous way of letting the police determine when search is called for without prior authorization by a magistrate."

J. ROBERT MESERVE.

LIE DETECTOR TEST EVIDENCE CANNOT BE USED DIRECTLY OR INDIRECTLY

If proper objection is made thereto, expert testimony deduced from a systolic blood pressure deception test popularly known as the "lie detector" test, is inadmissible in evidence in this state. *People v. Wochnick*, 98 A.C.A. 132 (1950). The Court thus adopted the same rule now followed in several other states, saying at page 136:

> "We are in accord with the views expressed in the foregoing cases that 'the systolic blood pressure deception test for determining the truthfulness of testimony has not yet gained such standing and scientific recognition as to justify the admission of expert testimony deduced from tests made under such theory'."

The Court further found that the admission of evidence indirectly involving results of the lie detector test was prejudicial error. California courts recognize that accusatory statements and the defendant's response thereto are admissible as an exception to the hearsay rule. In the *Wochnick* case, the prosecution introduced a statement by a police officer to the effect that the lie detector showed a strong reaction which usually indicates lying when certain critical questions were asked of the defendant. The defendant's response to this statement was also shown. The Court held that the statement was prejudicial, even though the court properly instructed that the results of the lie detector test were not to be used as evidence, but only as a basis for examining the defendant's response thereto. The decision was based upon the important influence the statement would have on a jury.

JACOB SWARTZ.

GROUNDS FOR DIVORCE— CAN INSANITY BE INCURABLE?

What proof is necessary to require the court to grant a divorce on the ground of incurable insanity? In *Wirz v. Wirz*, 96 A.C.A. 172, 214 Pac. (2d) 839 (1950), the local court had before it the uncontradicted and unimpeached testimony of the superintendent of the state mental institution, in which plaintiff's wife had been an inmate for more than eleven years, to the effect that "in the realm of reasonable probability the defendant would get progres-

sively worse and could never be released." Nevertheless, the trial judge found the defendant *not* incurably insane and specified that the plaintiff had failed to prove that his wife was "absolutely, incurably insane, and I don't think any human being can say that about anybody."

Although the judgment denying divorce was sustained on appeal on the ground that the plaintiff failed to satisfy the financial responsibility clause of Civil Code Section 108, the appellate court nevertheless, held that expert, uncontradicted and unimpeached, opinion evidence of "incurable insanity" could not, under Code of Civil Procedure Section 1826, be arbitrarily disregarded. The Court noted that on this issue the case was one of first impression in California. It cited *Tipton v. Tipton*, 309 Ky. 338, 217 S.W. (2d) 799 (1949), to support its reasoning that absolute certainty is not required with respect to the proof of "incurable insanity" and that if such certainty were required by the courts then the intention of the legislature would surely be defeated.

JAMES D. HARRIS.

CALIFORNIA MARITAL EXEMPTIONS

(Continued from page 5)

dents and their estates would move to a domicile more sympathetic to their economic problems, *e.g.* Florida.

There was also the reminder that prior to 1948 many people were disposing of their separate property by utilizing the trust, with a life estate for the surviving spouse, as a device for minimizing the overall death tax problem, both state and federal. In that way, all of the property was taxed at the husband's death,[7] but none was reached on the subsequent death of the wife.[8] With the advent of the marital deduction for federal estate tax purposes, many of these individuals altered their plans to give the surviving spouse a taxable power of appointment over the trust property, thus qualifying for the marital deduction. For federal purposes, only one-half of the property was then taxed on the death of each spouse. The reduced brackets produced the savings. This, in effect, resulted in a tax benefit to the State of New York. By thus qualifying for the federal benefits, these plans were subjecting all the family assets to a state death tax at the husband's death and one-half of the assets in the wife's estate thereafter. Some commentators considered it "unfair" for the state to benefit in this way from a federal provision designed to provide tax relief.[9]

California's reasons for enacting its new marital exemption have not been announced. Presumably, they would be the same as those of New York.[10] The tax savings would not be so great because of the predominance of community property passing from decedents who reside here. If the desire for uniformity was responsible for the new enactment in California, the result must disappoint those who conceived the plan. The new law provides

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[7]"Husband" as used herein refers to the first decedent, and "wife" refers to the surviving spouse.

[8]For a holding that trust corpus in which decedent had only a life estate is not includible in his gross estate, see Helvering v. Safe Deposit & Trust Co. of Baltimore, 316 U.S. 56 (1942).

[9]See Report cited at note 6, *supra*.

[10]California has one further reason. People who acquired personal property in other states, under circumstances that would cause it to be community property if they lived here, are treated as if it were community property if they die residents of California. See CAL. PROB. CODE §201.5. One line of argument presented to the legislature urged that this constituted tax discrimination against those who owned separate property and had always resided in this state. They were taxed on all of such property at their death without the benefit of either a community property or a marital exemption. While the validity of that reasoning and its finding of discrimination may be questioned in part, it did help to achieve its goal.

Of necessity, much of what is stated herein cannot be documented. The factors that influenced our legislature were discovered by discussions with individual members of that body.

an exemption, which is quite different from the deduction adopted elsewhere. It deals with transfers of property at death from one spouse to another, and it will enable a few individuals to save death taxes. Beyond that, our new exemption bears but slight resemblance to the federal marital deduction.[11]

II.

EXEMPTIONS, NOT A DEDUCTION

The California marital exemption, Section 13805 of the Revenue and Taxation Code,[12] provides:

> Exemptions—Transfer to decedent's spouse.—Property equal in amount to the clear market value of one-half of the decedent's separate property shall, if transferred to the spouse of the deceased, be exempt from the tax imposed by this part. A transfer, for the purpose of this exemption, shall include a transfer of property in trust with a general or limited power of appointment in the surviving spouse. This exemption shall be in addition to all other exemptions under this part.

The most obvious distinction between this new law and the federal provision is that California has an exemption and not a deduction. The federal estate tax allows a deduction, to the extent of one-half the value of the decedent's separate property, if there is a transfer to the surviving spouse under specified circumstances. The exemption results in a smaller saving in taxes than would a deduction. The latter removes the property from the taxable estate before the tax-rate brackets are applied. It, therefore, removes property from the highest tax bracket. The exemption, on the other hand, is applied after the tax brackets are determined. It removes property from the lowest bracket. An example of the difference in tax results will emphasize this. The following schedule sets forth the California inheritance tax payable on the estates indicated, under the prior California law, under the

[11]As originally recommended in California, the new law was to provide a marital deduction similar to that allowed under the federal statutes. Apparently a desire for simplicity and a consideration of the general probate attorney's problems in computing a complicated marital deduction caused the exemption to be adopted by the Legislature. The legislature passed an exemption during 1949, exactly like this year's law. The 1949 Bill (Assembly Bill No. 3111) was subjected to a pocket veto by Governor Warren.

On March 15, 1950, the same measure was introduced as Senate Bill No. 7. It was passed within a month.

The Inheritance Tax Department has estimated that the exemption will mean a loss in revenue to the state of approximately $400,000.00 per year. This will probably be reduced to some extent by the wealthy individuals who will be induced to remain in California because of this tax saving.

[12]Added by Laws of 1950, c. 5, §1; applicable to estates of decedents dying after April 26, 1950.

present law with the exemption and under the deduction as originally proposed. It is assumed that there is a bequest of the entire net estate to the surviving spouse and that it consists entirely of the decedent's separate property.

	CALIFORNIA INHERITANCE TAX PAYABLE		
Net Estate	Old Law	Present Law with a Marital Exemption	Proposed Law with a Marital Deduction
$ 25,000.00	$ 20.00	$ None	$ None
50,000.00	770.00	30.00	20.00
100,000.00	2,770.00	1,040.00	770.00
300,000.00	18,770.00	10,820.00	6,270.00
500,000.00	36,770.00	20,340.00	14,270.00
1,000,000.00	86,770.00	47,600.00	36,770.00

If we may speculate as to the purposes behind a legislative enactment, it is conceivable that this arrangement might have been a compromise. The tax savings are not as great as under a marital deduction, but the restrictions on the types of transfers which qualify for the exemption are negligible. Also, the statute is suspiciously concise for a revenue measure. Perhaps we give up tax dollars in exchange for a simple tax law.

III.

WHAT TYPE OF TRANSFERS QUALIFY FOR THE MARITAL DEDUCTION?

Let us recall briefly the prerequisites for the federal marital deduction. A husband's estate is entitled to a deduction, up to one-half the value of his separate property, to the extent that he leaves property to his wife outright, or under such an arrangement that she may be realistically considered its absolute owner. The detailed requirements which must be met to obtain this tax benefit have required tens of thousands of words of statutes, regulations and comment. In substance, the wife must receive such an interest in the husband's separate property that it will be taxable in her estate at death, unless, of course, it is dissipated or otherwise disposed of during her remaining years.

The California exemption, on the other hand, is equal in amount to the value of property transferred to the wife. Apparently the only restriction is that the exemption cannot exceed one-half the value of the decedent's separate property. There is no require-

ment that she receive an interest that would produce a tax at her death. Thus, a life estate, in trust *or otherwise*, with or without a power to appoint the remainder, would qualify.[13]

While a great deal of flexibility is thus available in planning an estate with an eye to the California inheritance tax, larger estates must consider the federal tax results and will still be influenced by the more rigid federal provisions. Therefore, it seems that those requirements will tend to control in the selection of testamentary plans for substantial estates. Of course, anything that would qualify for the federal marital deduction would also satisfy the requirements for the state exemption.[14]

Still, there may be instances where the peculiar nature of the assets, separate or community, is such that the reward of qualifying for the federal deduction is not worth the price in terms of actual control and ownership of the property. In such cases, the new exemption will be worthy of consideration. Some tax savings may be achieved under the state law without the complete disruption of a desirable testamentary plan.

Although this new provision may be "astringently short,"[15] it poses some questions which will require a definitive answer before complete reliance can be placed upon the inviting simplicity. The section states that a transfer, within the purposes of the exemption, includes a transfer of property in trust with a general or limited power of appointment in the surviving spouse. Does this imply that a transfer in trust unaccompanied by a power of any sort will not qualify for the exemption? It seems unlikely. Aside from the literal wording of the section itself, this conclusion seems strained when we consider the possible results of such an interpretation. It might be persuasive if the existence of such a

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[13]The statute's only requirement is that "property" be "transferred." Cal. Inh. Tax Reg. §616 defines "property" as follows:

> "Property," as used in these rules and regulations, includes any real or personal property, and any right or interest therein or income therefrom, the receipt or succession to which may be taxed under the inheritance tax and under the Constitutions of this State and the United States.

CAL. REV. & TAX CODE §13304 states:

> "Transfer" includes the passage of any property or any interest therein or income therefrom, in possession or enjoyment, present or future, in trust or otherwise.

The statement in the text seems obvious, under these definitions. Moreover, the unofficial conclusions of the Inheritance Tax Department attorneys are in accord.

[14]The existence of a "terminable interest," so fatal under the marital deduction [See INT. REV. CODE §812(e)(2)], does not preclude the exemption. Even a bequest that is conditioned on the wife's surviving distribution would seem to qualify. Of course, the valuation of such an interest would be affected and, correspondingly, the amount of the exemption.

[15]This pungent characterization was employed in Krystal, *Tax Notes*, 25 L. A. BAR BULL. 315 (1950).

power would cause the inheritance tax to reach the subject property at the death of the surviving spouse. But, in California, the donee's exercise of a power of appointment is not considered a taxable transfer.[16] Thus, no purpose would be served by such a construction of the new section. Moreover, it appears that a legal life estate given to the survivor would qualify for the exemption without reference to the existence of a power to appoint the property.[17] The reference to powers in the section is undoubtedly intended to dispel any fears that the federal requirements must be met to qualify for the state exemption.[18]

Another question presents itself. The statute provides that

> Property equal in amount to . . . the value of one-half of the decedent's separate property shall, if transferred to the spouse of the deceased, be exempt . . .

It does not say that property transferred to the surviving spouse will be exempt from tax, to the extent that it does not exceed one-half the value of the decedent's separate property. Is there a difference? To qualify for the exemption, must the decedent leave to his widow property sufficient to equal or exceed the value of one-half of his separate property? If that literal interpretation is placed upon the section, it is more than "astringently short"; it is dangerously misleading. Certainly, it was not so intended.

The new exemption presents a possible problem which is related to an old dispute under the federal law. There has been considerable question as to the federal estate and gift tax consequences of the following facts: Husband and wife have a substantial estate consisting entirely of community property; husband dies, and his will leaves all of the property in a trust, the provisions of which give a life income to the widow and remainders over to the children upon her death. The wife is put to an election between taking an equitable life interest in the entire estate or her community interest, *i.e.* one-half of the estate in outright ownership.

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[16]This statement applies where the donor of the power dies after June 25, 1935. The taxable transaction is now the giving of the power to the donee, not the latter's exercise thereof. See CAL. REV. & TAX. CODE §§13691 *et seq.*, and Cal. Inh. Tax Reg. §622. That this need not always be true, see Graves v. Schmidlapp, 315 U.S. 657 (1942); Estate of Newton, 94 Adv. Cal. App. 270, 210 P.2d 511 (1949) (hearing by Sup. Ct. granted). *Cf.* Federal law which specifically taxes a power of appointment as ownership of the subject property by the donee (with limited exceptions). INT. REV. CODE §811(f).

[17]This is completely contrary to the federal requirements. INT. REV. CODE §812(e)(1)(B), and U.S. Treas. Reg. 105, §81.47b. See note 13, *supra*.

[18]Apparently the wife could be given a life interest in a trust the income of which was to be accumulated. This would qualify for the exemption. The value would be affected and, accordingly, the extent of the exemption.

She elects to take under the will. Has she thereby transferred her half of the community property in trust, irrevocably, reserving to herself a life estate therein? If so, she is subject to an immediate federal gift tax on the value of the remainder in her half of the property.[19] Moreover, the property is includible in her estate at death and taxed again.[20] The Bureau of Internal Revenue presently indicates, informally, that it will so treat the above transaction. Section 79 of the California Gift Tax Regulations expressly disclaims any intention to find a taxable gift in the above situation, and, presumably, this election causes no state inheritance tax at the wife's death.

Some writers have suggested that the wife, for federal purposes, exchanges the remainder in her half of the property for a life estate in the husband's half.[21] By determining the values of these respective interests under the mortality tables, we may ascertain the value of the remainder given by the wife in excess of the value of the life interest she received. It is generally argued that only this excess, if any, should be subject to federal gift and estate tax, and that the balance constitutes an exchange for equal value or a sale. If this theory should be officially adopted, the property "transferred" (meaning a taxable transfer) by the husband to the wife would be of a negligible value. California reaches this result by gift tax regulation. If the basis for that ruling is the reasoning outlined above, the marital exemption allowed to the husband's estate on this disposition would be insignificant, *i.e.* the excess of the value of her equitable life estate in the husband's half of the community property over the value of the remainder after her life estate in her half. In fact, in most cases, the remainder will be worth more than the life estate. To obtain any marital exemption, then, it would be necessary for the husband to leave the wife some interest in his separate property. Fortunately, there is little to indicate that California will take this approach.[22]

One further provision in this new section should be noted. The

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[19]That is, the value of the property, less the value of the retained life estate.

[20]INT. REV. CODE §811(c). For a brief discussion of this problem, see Nossaman, *Drafting a Testamentary Trust;* 1948 MAJOR TAX PROBLEMS, U.S.C. TAX INSTITUTE 115, 1949; Brown and Sherman, *Election to Take by Will,* 23 CAL. S. B. J. 150 (1948).

[21]See Brown and Sherman, *op.cit. supra,* note 20.

[22]As the gift tax regulation cited above shows, California has been lenient, taxwise, with these "election" situations. There is no reason to anticipate a change in this policy.

"clear market value" of the separate property is the guide by which the maximum exemption is determined. This refers to the market value of the separate property less the total deductions prorated against such assets. This method of determining the extent of the exemption in the individual case appears to have considerable merit, when compared to the federal concept of the "adjusted gross estate."[23]

IV.

CONCLUSIONS

Whatever the defects that may be discerned by the eager tax advocate, the California marital exemption represents a commendable step toward fairness between separate and community property. It is unfortunate that our state gift tax law was not similarly favored by legislative attention.[24]

This exemption will probably result in a smaller reduction in the state revenues than has been anticipated. Much of the separate property of this state is treated, for inheritance tax purposes, as community property, by reason of the *"Tomaier* rule."[25] Since the community property exemption continues to be much more inviting than the inheritance tax treatment of separate property, even with the marital exemption, we may expect to see the latter utilized only when success under the *Tomaier* rule is hopeless because of adverse evidence or a widow reluctant to testify that she and her deceased husband had always referred to the property in question as "ours." The exemption, nevertheless, does represent an important factor to be taken into account in the process of planning for the testamentary disposition of property.

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[23] INT. REV. CODE §812(e)(2).

[24] Although most people consider the state gift tax as a relatively insignificant item, it actually imposes a greater levy than the federal gift tax in many situations. This is true because of the difference in exemptions under the two taxes, as well as the special treatment accorded to gifts by and between spouses under the Revenue Act of 1948. INT. REV. CODE §§1000(f), 1004(a)(3). The following examples will indicate the extent of California's "discrimination" against owners of separate property. The examples assume a gift of the indicated amount to a non-relative by a married person who has made no previous gifts of substantial amounts during his lifetime.

Amount of Gift	*Federal Tax*	*California Tax*
$ 50,000.00	$ None	$ 3,846.50
100,000.00	1,905.00	9,766.50
200,000.00	17,190.00	21,766.50

[25] Tomaier v. Tomaier, 23 Cal.2d 754, 146 P.2d 905 (1944). The language of that decision has been held responsible for the present practice of treating jointly owned assets as community or joint-tenancy property according to the whim and tax consciousness of the surviving spouse. It is said that record title will not control the status of property held by spouses. Oral evidence is admissible to indicate their intention and the "true" status of such property.

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SALE OF A RETAIL BUSINESS

(Continued from page 7)

condition against assigning or subletting without the landlord's consent. As a result the buyer may find himself with a good enough business, but nowhere to conduct it. Or, in order to hold the premises, he may be forced to pay a higher rental than he had planned. To make matters worse, the landlord may in some circumstances plausibly claim that he became the owner of the fixtures installed by the seller.[13] The lessons are obvious.

E. *Taxes.* Without exception the seller's unpaid taxes are matters of concern to the buyer. The buyer is personally liable for unpaid city and state sales taxes[14] and unpaid state unemployment insurance contributions.[15] Unpaid federal taxes are a lien upon the seller's real and personal property rights[16] which is valid as to subsequent purchasers if filed for record with the County Recorder.[17] Unpaid state income taxes, personal and corporation, are also a lien upon the seller's real and personal property from the time of filing for record with the County Recorder.[18] Unpaid real and personal property taxes become a lien on the seller's real property as of lien date.[19] Therefore, the buyer should insist on escrow instructions which require the seller to obtain releases as to federal taxes, including income, withholding, social security, and excise taxes,[20] state taxes including unemployment insurance contributions,[21] income,[22] sales,[23] and property taxes[24] and city sales and license taxes.[25] Circumstances may also indicate the desirability of checking as to gift and inheritance taxes.

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[13]CAL. CIV. CODE §1019 (on the ground that thing affixed has "become an integral part of the premises"); *cf.* Alden v. Mayfield, 163 Cal. 793, 127 Pac. 44 (1912) (involving plate glass window).

[14]L. A. City Ordinance No. 90360, as amended, §21.199(j); CAL. REV. & TAX. CODE §6812.

[15]California Unemployment Insurance Act §45.7.

[16]INT. REV. CODE §§3670, 3671.

[17]INT. REV. CODE §3672; CAL. GOVT. CODE §§27330-27332.

[18]CAL. REV. & TAX. CODE §§18881-18885, Corp. Income Tax Act of 1937 §22.

[19]CAL. REV. & TAX. CODE §§2187-2189, 2192.

[20]Releases as to all federal taxes may be obtained from the Collector of Internal Revenue, Legal Section, Escrow Section, P.O. Box 391, Los Angeles.

[21]Release may be obtained from the office of the State Department of Employment in the district in which the business is located.

[22]Release as to personal income tax may be obtained from the State Franchise Tax Board, Room 204F, State Building, Los Angeles. Release as to corporation income tax may be obtained from the Board at 1025 P. Street, Sacramento.

[23]Release may be obtained from State Board of Equalization, Room 210, 357 South Hill Street, Los Angeles.

[24]Seller should produce tax receipts or a release which may be obtained at rooms 302, 308, Hall of Justice, Los Angeles.

[25]Releases may be obtained from Close-out Section, Room 1, City Hall.

F. *Other Claims.* In the usual case the buyer does not wish to assume the liabilities of the seller, and the sale contract should make this clear. Then, if statutory notice of the sale is given under California Civil Code Section 3440[26] and the sale is completed as published,[27] the buyer will not be affected by claims of the seller's unsecured creditors. Accordingly, the buyer should demand escrow instructions which require delivery of documents of title to him upon his performance irrespective of the existence of disputed claims of seller's creditors upon the escrow holder.

G. *Good Will.* From the buyer's viewpoint, essential features of the contract of sale are the transfer of good will and the seller's covenant not to compete. There is no doubt about the enforceability of such provisions if the restrictions upon the seller are properly limited as to time and space.[28]

II. THE SELLER

A. *Securing the Purchase Price.* Whereas the buyer is embarking upon a venture for profit, the seller is getting out. His concern lies in liquidation of his holdings as rapidly and inexpensively as possible. If he cannot sell for cash, he wants a satisfactory device to secure the unpaid purchase price.

The property being sold will ordinarily include fixtures and store equipment. A chattel mortgage upon such property is a permissible security transaction and may be more acceptable to the buyer than a conditional sales contract. Such a chattel mortgage should be made substantially in the form prescribed in Section 2956 of the California Civil Code and should be recorded with the County Recorder in conformity with California Civil Code Section 2957. The recordation must be accomplished within a reasonable time.[29]

Among local practitioners there appears to be a well-established assumption that a notice of intention to give a purchase money chattel mortgage must be recorded and published under California

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[26]CAL. CIV. CODE §3440 now requires recording of notice at least 10 days in advance of the sale and publication at least 5 days in advance. Forms are available at legal newspapers.

[27]CAL. CIV. CODE §3440; Mitchell v. Setzler, 84 Cal.App.2d 716, 191 P.2d 523 (1948).

[28]CAL. BUSINESS AND PROFESSIONS CODE §§16,600, 16,601.

[29]Ruggles v. Cannedy, 127 Cal. 290, 53 Pac. 827 (1899). Citizens Nat. Tr. & Sav. Bk. v. Gardner, 161 F.2d 530 (9th Cir. 1947).

Civil Code Section 3440. Federal courts, construing Section 3440 and its New York counterpart in bankruptcy cases, have held that purchase money chattel mortgages on fixtures and equipment are good against the buyer's trustee in bankruptcy in spite of non-compliance with the Bulk Sales Act, if properly recorded under California Civil Code Section 2957.[30] If these cases are regarded as controlling, then giving of notice of such intended mortgages is an expensive, time consuming, and needless gesture and may be omitted from escrow procedure.

Property being sold will also ordinarily include stock in trade. Whether a purchase money chattel mortgage on this class of property will protect the seller is an open question. California Civil Code Section 2955 provides:

> Mortgages may be made upon . . . all kinds of personal property, except the following: . . . 3. The stock in trade of a merchant. . . .

In recognition of this Section, California Civil Code Section 3440 provides that proper recordation and publication of notice will insulate a mortgage of fixtures and store equipment against a mortgagor's creditors, but contains no such provision as to mortgages of stock in trade.

However, as has been noted, validity of purchase money chattel mortgages does not appear to depend upon compliance with California Civil Code Section 3440.[31]

Further, a statute in Texas similar to California Civil Code Section 2955 has been held not to invalidate a purchase money chattel mortgage on stock in trade.[32] If such a statute is intended to protect only existing creditors, the Texas decision would seem to be correct, since the existing assets, on which credit was extended, are not depleted by a purchase money chattel mortgage. If, however, it is intended to make it possible for prospective creditors of the merchant always to be able to rely upon the freedom of merchandise from preferential plasters, then the source of the security is immaterial, and the Texas decision would seem to

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[30]Citizens Nat. Tr. & Sav. Bk. v. Gardner, *supra*, note 29; *In re* Mercury Engineering, Inc., 68 F. Supp. 376 (S.D. Cal. 1946); *In re* Rosom Utilities, 105 F.2d 132 (2d Cir. 1939).

[31]See note 30 *supra*.

[32]Bowen v. Lansing Wagon Works, 91 Tex. 385, 43 S.W. 872 (1898).

be incorrect. The California courts have not passed upon the question.

If stock in trade is intended to constitute a portion of the security, the seller, if his bargaining position will permit, would be well advised to demand the use of a conditional sales contract rather than a chattel mortgage. A trust receipt, while authorized only upon items entrusted for the purpose of resale,[33] may also be satisfactory to the parties where stock in trade is intended to constitute the entire security. California courts recognize and uphold the distinctions between chattel mortgages and conditional sales[34] and trust receipts.[35]

Although retention of a security interest in stock in trade furnishes protection which is better than none, the seller should realize that it will diminish in value. It is customary to sell the oldest goods first. A successful business means a rapid turnover of stock. Any attempt to extend the mortgage to cover merchandise which replaces the original stock will fail.[36] Moreover, a serious problem of identifying mortgaged stock will exist after partial replacement. This may be met in part by requiring the buyer to use accurate inventory methods.

B. *Taxes.* The seller's tax liabilities arising out of conduct of the business are already fixed at the time of the sale. But he should know that a sales tax liability arises out of the sale itself[37]

[33]CAL. CIV. CODE §3014(3)(a).

[34]Bice v. Harold F. Arnold, Inc., *supra*, note 8.

[35]Commercial Discount Co. v. Los Angeles, 16 Cal.2d 158, 105 P.2d 115 (1940); Chichester v. Commercial Credit Co., 37 Cal.App.2d 439, 99 P.2d 1083 (1940).

[36]CAL. CIV. CODE §2955 covers this squarely.

[37]Ruling No. 81 of Sales and Use Tax Rules and Regulations interprets §§6006.5, 6015, and 6367 of REV. & TAX CODE to require payment of sales tax upon sale of fixtures and store equipment (but not upon sale of items sold for resale).

in order that he may require the buyer to agree to pay it[38] or to consider it in fixing his asking price.

A promissory note should always be required by the seller in conjunction with a conditional sales contract or by the entruster in conjunction with a trust receipt. A solvent credits tax is imposed upon the amount of the obligation represented by such instruments in the absence of a concurrent note.[39]

C. *Funds Held by Escrow Holder.* A survey of form escrow instructions in common use in this city shows a uniform authorization to the escrow holder to withhold purchase money from the seller indefinitely, in some instances equal to 150 per cent of the amount of claims which have been disapproved by the seller, pending settlement of such claims, and to file an action of interpleader at the expense of the buyer and the seller. Parties to the sale, particularly the seller, should realize that they are not required by law to provide for settlement of claims, approved or disapproved, through escrow, and that such provisions are inserted in the form instructions by the escrow holders to protect themselves from the expense of defending baseless lawsuits by unsatisfied claimants. California Civil Code Section 3440 is intended to give notice to the seller's creditors in order that they may take steps to have their accounts paid. But the mere filing of a claim with an escrow holder creates no lien upon the funds. In the absence of attachment or execution, the escrow holder may pay over funds without liability.[40] Upon request some escrow holders may be willing to operate under instructions to disregard unapproved claims.

III. SUMMARY

The buyer should be satisfied as to title to the property being sold, tax liens, and other security interests therein, the lease, compliance with California Civil Code Section 3440, and a covenant not to compete. The seller should receive valid security for the purchase price, protection against tax due to the sale, and reasonable terms for escrow.

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[38]The buyer is not liable to the seller in absence of contract. National Ice & Cold Storage Co. v. Pacific Fruit Exp. Co., 11 Cal.2d 283, 79 P.2d 380 (1938). However, the buyer is liable for the tax if the seller does not pay it. See note 14 *supra*.

[39]CAL. REV. & TAX. CODE §§112, 113, 2153. Cases cited note 34 *supra*.

[40]See Orloff v. Metropolitan Trust Co. of Calif., 17 Cal.2d 484, 110 P.2d 396 (1941).

BURDENS OF PLEADING AND PROOF

(Continued from page 9)

There are three standard answers in title actions. The defendant may plead facts in his answer which show legal or record title in him, plus an allegation of *bona fide* purchase. He may plead facts showing some other type of interest, plus an allegation of *bona fide* purchase. Or he may only deny the plaintiff's allegations of title and affirmatively allege that he is a *bona fide* purchaser, without setting out his chain of title.

In the opposite situation, a suit by an alleged *bona fide* purchaser, such plaintiff should make every effort to state a chain of title showing legal title in himself. The answer will generally deny his title, and may or may not challenge his status as a *bona fide* purchaser.

The party who seeks the protection of the *bona fide* purchaser doctrine must plead it with exactitude[7] in every case, except those instances where the statutory replication supplies his pleading. But, as to the *bona fides,* the burden of proof will not always follow the burden of pleading—another instance where the comfortable old saw is untrue.

B. BURDEN OF PROOF

The burden of proof on the issue of *bona fide* purchase falls upon the party challenging the rights of the present legal or record title holder. Depending on the facts and the state of the pleadings, the one alleging legal or record title may be either plaintiff or defendant and may or may not allege *bona fide* purchase. In any case, the one attacking the legal title holder will bear the burden of proof: either to prove that he himself is a *bona fide* purchaser for value without notice, or that his opponent is lacking those qualities necessary for that protected position.

A brief review of two lines of cases will illustrate situations in which the assignment of this burden of proof becomes a turning point of the decision.

1. "Trust" Cases.

One group of cases in which the burden has been thrust upon the party attacking the *bona fides* of the other, has been described

[7]California Cured Fruit Ass'n v. Stelling, 141 Cal. 713 (1904).

as cases of resulting or constructive trusts.[8] The majority of these cases did involve such alleged trusts, but the rule is not confined to that field, nor is the trust allegation the reason for the rule. The distinguishing feature of such cases is that the alleged *bona fide* purchaser also had the present legal or record title. Probably the first case to state the rule, *Wyrick v. Weck*,[9] was an action to declare a constructive trust of certain land. The plaintiff alleged that her father, who had received a certificate of purchase for the land, died intestate, leaving his widow and plaintiff surviving him. With the record title still in the decedent, the widow purported to sell the certificate to X, who procured a patent. Thereafter, the defendant took title by grant deed from X, allegedly with full knowledge of the facts. After making these allegations in her complaint, thus showing legal title in defendant, the plaintiff offered no evidence during the trial of notice to, or knowledge by, defendant of plaintiff's equities. The trial court's judgment of non-suit was affirmed by the Supreme Court.

In another case the complaint contained allegations that plaintiff had provided half the purchase price of the land to his brother, who took title in his own name but held it in secret trust for plaintiff and that the brother later sold the land to X, who completed the purchase with full knowledge of plaintiff's equity. Judgment was for X on the ground of *bona fide* purchase. Plaintiff had failed to sustain the burden of showing that defendant was not a *bona fide* purchaser; that is, that he had sufficient notice of matters outside the record title which would establish a constructive trust in plaintiff's favor.[10]

In *Dimity v. Dixon*,[11] the complaint alleged defendant took title to partnership realty knowing that his grantor held legal title as a partner in trust for the partnership, through which plaintiff claimed. The court found plaintiff's evidence insufficient to meet the burden of proof as to defendant's notice of the trust, or lack of consideration. A more recent and authoritative case of *bona fide* purchase of partnership property followed the same rule as to

[8]25 Cal. Jur. 846.
[9]68 Cal. 8 (1885).
[10]Kowalsky v. Kimberlin, 173 Cal. 506 (1916), relying on CAL. CIV. CODE §856.
[11]74 Cal.App. 714 (1925).

burden of proof.[12] The court emphasized the provisions of Civil Code Sections 2404 and 2403(1), part of the Uniform Partnership Act, as statutory support for the rule.[13]

Additional cases that placed the burden of proof on the party attacking the legal or record title involved: (1) A conveyance by an insolvent debtor to his brother, allegedly in fraud of creditors and on secret trust for the debtor, and thence to plaintiff, who successfully quieted his title as a *bona fide* purchaser;[14] (2) conveyance to a corporation, which quickly conveyed the land to defendant without giving a purchase money note and mortgage to plaintiff grantor;[15] (3) heirs taking title under a final decree of distribution of a decedent's estate, after allegedly concealing the existence of the plaintiff, another heir, from the probate court;[16] (4) conveyance by a joint tenant of the property to a third person;[17] and (5) retention of the land by an optionor, after the express duration of the option expired without exercise by the optionee, who failed to sustain the burden of establishing his *bona fides* against the optionor's legal title.[18]

2. Prior Unrecorded Deed Cases.

The other major line of cases holds that the burden of proof is on one claiming to be a *bona fide* purchaser. These are cases in which such party has only an equitable or, at least, non-legal, title. The line between these two types of cases was succinctly described by Justice Shaw in the leading case, *Bell v. Pleasant*,[19] but his words have not been given much weight, judging by the volume of reported cases on the subject since his opinion. He held that a party claiming to be a good faith purchaser under a deed executed after, but recorded prior to, a grant deed by the same grantor had the burden of proving himself a *bona fide* purchaser.

> "There is a line of cases which the defendants contend establish a contrary rule, but upon examination it will be

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[12]Barton v. Ludy, 11 Cal.2d 1 (1938).

[13]Now CORP. CODE §§15010 and 15009(1) which provide that conveyance by the partner holding title passes the title unless the purchaser has knowledge that the partner has exceeded his authority.

[14]Casey v. Leggett, 125 Cal. 664 (1899).

[15]Hawke v. Calif. Realty & Construction Co., 28 Cal.App. 377 (1915).

[16]Ferguson v. Ferguson, 58 Cal.App.2d 811 (1943).

[17]Pellerito v. Dragna, 41 Cal.App.2d 85 (1940). (The purchaser bears the burden of proof to overcome the legal title to a half-interest remaining in the other joint tenant—vice versa as to the other half.)

[18]Oswald v. Northrop Aircraft Co., 62 Cal.App.2d 824 (1944).

[19]145 Cal. 410 (1904).

> seen that there is a clear distinction between them and the case at bar. . . . The underlying reason for this rule in these cases is, that as the debtor or trustee, as the case may be, holds the legal title at the time of the conveyance, the legal effect of his deed is to convey that title to his grantee, and thus there is established a legal condition which inures to the benefit of the grantee and cannot be changed in equity, except by proof of circumstances to show a superior equity in the party who disputes it. Equity follows the law, and a legal condition or status being once established, the burden of proof of facts necessary in equity to change the status is upon him who asserts the equitable right . . . In the case at bar and other similar cases, however, the conditions are precisely the reverse and the principle operates against the defendant."[20]

The largest number of cases in which the burden of proof has been assigned to the alleged *bona fide* purchaser to prove his good faith, lack of notice or knowledge, and payment of value, likewise involve the opponent claiming under a prior unrecorded deed. The standard situation is a landowner conveying the property to A by grant deed, A failing to record, the landowner then conveying the same property to B, who records before A finally does so. Either A or B then brings an action to quiet title, and B alleges *bona fide* purchase. The courts strongly enforce the rule that the burden is upon B to prove his status, because the legal title and *prima facie* right is in A. The theory is that the grantor's deed passed good title to A, and this title was not voided by any provi-

[20]145 Cal. 410, 415 (1904). This theory behind placing the burden of proof as to *bona fide* purchase has not been better stated. The ancient equity maxim of equity following the law is readily applicable in suits by or against alleged *bona fide* purchasers, because such suits are generally equitable in nature.

sion of the Recording Act, which merely states the status of unrecorded deeds followed by *bona fide* purchase by another.[21] The grantor had no title to pass by his second deed to B, and B merely had an equitable interest, which could ripen into legal title only if he proved his status as a *bona fide* purchaser.[22]

In one case involving a prior unrecorded deed, the court refused to place the burden of proof on the holder of the subsequent deed. The subsequent deed holder was the plaintiff, who alleged his chain of title in full. The defendant entered only a general denial and alleged it was the owner in fee. The defendant did not introduce or refer to the prior unrecorded deed to it until its case in chief. The court felt that the defendant's silence about his prior unrecorded deed was unfair, and a surprise to plaintiff, and, in connection with several other circumstances of bad faith, it justified placing the burden of proof on defendant.[23] The moral, as to pleading, for a holder of a prior unrecorded deed is obvious.

Further situations in which the burden of proof has been placed on the alleged *bona fide* purchaser to prove his worth, because he was attacking the legal title, are: (1) suit by a record heir of a townsite settlor, who, as heir, was entitled to an undivided interest in land, against a purchaser from the holder of the actual patent, which had been granted in the name of another heir;[24] (2) suit by an assignee of a prior contract of sale of land against a purchaser under a subsequent contract, which subsequent contract was executed after the plaintiff had tendered the amount due and demanded conveyance from the vendor (thus putting legal title in plaintiff);[25] (3) suit by heirs of the former owner against a purchaser claiming under a conveyance of one holding a power of attorney from the heirs, but which conveyance was outside the power and void;[26] and (4) suit by an alleged *bona fide* purchaser against a lessee under a lease executed prior to plaintiff taking

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[21]CAL. CIV. CODE §§1214, 1217.

[22]Bell v. Pleasant, 145 Cal. 410 (1904); Long v. Dollarhide, 24 Cal. 218 (1864); Wilhoit v. Lyons, 98 Cal. 409 (1893); County Bank v. Fox, 119 Cal. 61 (1897); Chapman v. Ostergard, 73 Cal.App. 539 (1925); Kenniff v. Caulfield, 140 Cal. 34 (1903); Olson v. Cornwell, 134 Cal.App. 419 (1933); *cf.* Hall. v. Chamberlain, 31 Cal.2d 673 (1948) (prior unrecorded deed prevailed over tax deed).

[23]Purcell v. Victor Power & Mining Co., 29 Cal.App. 504, 514 (1916).

[24]Eversdon v. Mayhew, 65 Cal. 163 (1884).

[25]McLane v. Storr, 75 Cal.App.2d 459 (1946).

[26]Alcorn v. Buschke, 133 Cal. 655 (1901).

title to the property, and of which plaintiff admitted knowledge in his complaint.[27]

The burden of proof is placed on the *bona fide* purchaser not holding the legal or record title even though the other party claims under a quitclaim deed,[28] and even though the title instruments are mortgages or trust deeds, rather than grant deeds.[29] The burden applies both to negativing knowledge or notice of the other's interest, and to proving valuable consideration.[30]

This review of the cases has dealt only with the assignment of the burden of persuasion, not with the burden of going forward with the evidence. The party assigned the burden of proof may meet it by sufficient evidence; the burden of going forward will then shift to the other party, whose evidence may sufficiently rebut the first party's to justify a finding against him.

[27]Isenhoot v. Chamberlain, 59 Cal. 630 (1881).
[28]United States v. Certain Parcels of Land, 85 Fed. Supp. 986 (D.C.S.D. Cal. 1949).
[29]Olson v. Cornwell, 134 Cal.App. 419 (1933); Hibernia S. & L. Society v. Farnham, 153 Cal. 578 (1908); County Bank v. Fox, 119 Cal. 61 (1897).
[30]James v. James, 80 Cal.App. 185 (1926).

C. SUMMARY AND CONCLUSION

The lessons to be learned by the practicing attorney from the review of California authorities are quite clear. (1) Before drafting the complaint or answer, as the case may be, the attorney should take a hard and critical look at the present title of each party. He should try to ascertain which party has the present legal title, according to the law of real property. (2) He may then proceed on the rule that the burden of pleading *bona fide* purchase, or the lack of it, will be on the party without the legal title. (3) This burden may perhaps be avoided by adroit pleading. If the plaintiff faces a potential *bona fide* purchaser, he should not show legal title in such defendant. If the plaintiff claims as *bona fide* purchaser, he should state legal title in himself, if possible. By the same token, the defendant should show legal title in himself, if plaintiff has been silent on the subject. In short, the party should show legal title in himself if at all possible, and absolutely avoid showing it to be in his opponent.

On the trial, the attorney may assume that California law assigns the burden of proof concerning *bona fide* purchase to the party attacking the right of the legal title holder to the property. If the attacker claims to be a *bona fide* purchaser, he must prove that he had no knowledge or notice of the other's legal title, a most difficult matter, and that he gave good consideration and acted in good faith. If he attacks one who is both a *bona fide* purchaser and legal title holder, he must positively prove, not only the defects in the other's title such as fraud, undue influence or mistake, but also notice, or knowledge of sufficient facts to put a prudent man on notice,[31] lack of consideration, or bad faith.

However, because of the frequent difficulty of determining which party has present legal title (record title is usually legal title, but both parties may have a title of record), justifiable caution dictates that each party assume that he has the burden of proof. Each should introduce sufficient competent evidence to sustain a finding in his favor. The prudent attorney will not stand back, believing that his opponent will have to struggle along with the burden of proof, except in the most standardized situations outlined above. The imprudent attorney may still be standing there with his burden down when judgment is rendered against him for failure to carry it.

[31] CAL. CIV. CODE §19; Kenniff v. Caulfield, 140 Cal. 34 (1903).